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THE CATTLE-LOAN COMPANY

I. INTRODUCTION

In the face of an insufficient European food supply we are today called upon to furnish beef in large quantities to the allied armies. Even before the outbreak of the present war beef production was a serious problem in the United States. From 1909 to 1915 the amount of production decreased from 0.56 to 0.366 beef animals per capita, and with some increase in production reached only 0.397 in 1917. The need for an intensified production of beef cattle in this country will not end with the closing of the war; it will continue even beyond the period required for the rehabilitation of the beef-ravaged countries of Europe. Since it has been estimated that about 75 per cent of all cattle operations are carried on by means of borrowed capital, it can readily be seen that cattle production is essentially dependent upon adequate financing.

In the early days, when the settlement of the territory east of the Mississippi was taking place, there was very little need for the extension of credit. The opening of the vast territory west of the Mississippi, which became available to the cattle grower at a merely nominal price, gave a great impetus to the cattle industry. Commission companies established in the meat-packing centers realized the opportunity to earn profits and to control the industry by lending money to the cattle-men. Equipped usually with small amounts of capital, and with no adequate system of inspection and supervision, they lent money widely and injudiciously. The industry of this period was very chaotic. The cattle themselves were "longhorns," a wild, inferior feeding type; the ranches were unfenced and cattle "rustling" was common; enormous losses resulted from insufficient water in summer and lack of feed in winter. Eventually the range became overstocked, and in 1895 and the few years following, the cattle

raisers suffered such heavy losses that they were unable to repay the loans, causing widespread failure among the commission firms doing business at that time. Cattle paper became very unpopular, and the stigma remained for many years. The present period of cattle financing began at about the opening of the twentieth century. While pasture lands have decreased to a pitiful fraction of their former size, the transition has brought system and stability to the cattle industry. The ranches are now practically all fenced, the cattle are an improved type, disease is well controlled, and "rustling" is over. Water is supplied by engines or Artesian wells, and adequate feed is stored for the winter. Skilled executives trained in approved business methods administer the affairs of the modern ranch. Cattle raising has become a specialized industry.

There were about three classes of institutions lending to cattle growers in the early part of the century: (1) the small state banks over the country, which were limited in their loans to 25 per cent or less of their capital stock and surplus, and which could seldom accommodate any except the small local feeder or grower; (2) a few large commission firms which lent almost altogether on feeder cattle, with the object of increasing the commission business; (3) the large national banks, limited to 10 per cent of their capital and surplus in their loans to any one person, unable to accommodate many of the large ranchmen, and with no credit machinery to inspect and supervise distant loans after they had been made.

Thus the national credit structure lacked a form of organization which could make unlimited loans on cattle, and which possessed machinery for adequate investigation of prospective loans and careful supervision of consummated loans. It lacked, moreover, a form of organization that could serve the cattlemen as a broker between the borrower and the investor, and thus distribute the available capital into the proper channels. Cattle-loan companies which could perform these necessary functions have existed in various forms for many years, but only in the past decade have they increased rapidly in numbers and attained a great perfection of organization.

II. TYPES AND LOCATION OF CATTLE-LOAN COMPANIES

Modern cattle-loan companies are divided generally into independent companies and those affiliated with state or national banks. The capital stock and surplus varies from \$25,000 to \$750,000. This is usually subscribed, in the case of the affiliated companies, by the directors and stockholders of the allied bank, and in certain cases friends of the men who are subscribing the majority of the capital stock have been admitted. The independent concerns as a rule have a smaller amount of capital stock, although there are a few independent companies throughout the country that are as large as the allied organizations. The independent companies, moreover, do not possess several distinct advantages which belong to companies affiliated with a strong bank. Generally, therefore, they are not as strong financially as the allied institutions.

In the case of a loan company connected with a large bank, the officers and their staff are as a rule also officers of the bank. Since, however, they are chosen because of their superior knowledge of every angle of the cattle industry and cattle loaning, independent companies often have as competent executives and staff as are the allied loan companies.

The majority of the best loan companies, both affiliated and independent, are incorporated. While many are organized and incorporated within the state in which they operate, it is rumored that the majority are incorporated in the state of Delaware.¹ This is probably true and is due to the advantages of smaller taxes, smaller organization fees, and certain legal advantages given by Delaware. There is an occasional institution that is organized as a joint-stock company. The affiliated companies are usually connected with some of the large live-stock national banks located in every packing center in the United States and ordinarily owned and controlled by some of the large packers.

A large majority of the companies are located in the chief packing centers. These, together with the ones on the Pacific coast and those in New Mexico, constitute practically all of the large companies in the United States. It is in the meat-packing

¹ The truth of this statement could not be confirmed because of unsystematic filing in the office of the secretary of that state.

centers that most of the live-stock business is concentrated, for it is here that the stockmen naturally go in search of money. There is the advantage in such a location that it is often possible for the loan company to inspect the cattle to be purchased in the market. It is also an advantageous position in which to guard against the illicit marketing of cattle by dishonest borrowers. Moreover, these centers are the vantage-points from which all important events and movements affecting the cattle industry are best observed. And finally, since the packers were the first to discover the opportunity to establish cattle-loan companies, it was logical and easy to connect them with the existing live-stock banks, using the same building and officers.

III. TYPES OF CATTLE LOANS

Loans made by cattle-loan companies are divided generally into three classes. These comprise: (1) feeder loans, (2) stocker loans, subdivided into loans on cows, loans on young stock, and "summer loans," and (3) dairy loans.

Feeder loans are made on beef steers which are ready to go into the last stage of feeding prior to their sale as finished beef. Their age will vary in different regions according to the custom of feeding either young or aged steers for market. Loans on feeder cattle are made to mature within ninety to one hundred and eighty days, according to the age of the steers and the length of time they are to be fed. Loans of this type are usually not renewed. The interest rate will vary according to the region under consideration, the conditions of the money market, and the conditions surrounding each individual case. As a general rule, however, the rates will average from 8 to 9 per cent in the West and Northwest, and from 6 to 8 in the Central West.

It is customary to lend occasionally as much as 100 per cent of the purchase price of cattle for feeding. In such cases the cattle must be considered of good quality, and the borrower must be a good moral risk with ability. He must have adequate watering facilities and shelter and sufficient feed to fatten the cattle completely. It is usually insisted that the feeder show enough additional responsibility to protect the company fully, for he must

assume (1) the expense of feeding and handling, (2) interest on the borrowed money, (3) all expense incidental to moving to market, and (4) all the risks concerning declining markets, disease, and other contingencies. If the risk does not warrant a loan for the entire price of the cattle, it may be scaled down to as low as 80 per cent of the total value.

Paper based upon loans on feeder cattle is extremely popular. The chief reason for the preference for this class of loans is their extraordinarily liquid nature. Feeder cattle are kept only a short time, never exceeding one hundred and eighty days, and are then marketed and slaughtered. To the investor who buys paper with a maturity of six months these loans perhaps appeal more strongly because in the event that it becomes necessary to go beyond the loan company to the borrower for the payment of the loan this will be less difficult when the cattle are ready for consumption. From the viewpoint of the commercial banker it is certainly the most desirable class of loans.

In addition, loans on feeder cattle become more valuable each day, as a steer on full feed will put on from one and one-half to two pounds of flesh daily. As the animal becomes heavier the quality of the beef also improves and the value of the steer is doubly increased. Steers in the feed lot are not subject to the same vicissitudes of the weather, disease, and accident as are stocker cattle. Paper based on loans upon feeder cattle possessed of these advantages ranks with the best commercial paper.

One division of stocker loans is made upon breeding stock. This does not include registered herds, for the reason that the amounts necessary for each individual animal and the risks attendant on such loans are too great for the cattle-loan companies to assume. Loans on cows to be used as breeding stock are made for six months' time and may be renewed from two to four times if the conditions surrounding the loan continue to be favorable. The margin required on such loans will vary according to the same factors that enter into the making of feeder loans. These loans are considered long-time advances. Cattle of this sort are not so easily marketed as feeder cattle, the loans are not liquid, and the margin of safety required is greater than for loans on feeder steers.

The percentage advanced on such loans may be roughly stated as about 50 to 60 per cent of the total value of the cows. The most desirable feature about these loans is the fact that the mortgage given on the cattle, as security for the loan, applies to the offspring. Thus not only does the security increase in value, but as the calves are sold the notes are liquidated. A loan made for eighteen months on a good herd of breeding cows will practically always be liquidated by the sale of the natural increase alone.¹

Stocker loans of another sort are those made upon young steers and heifers intended ultimately to be marketed. These are also made for periods of six months, with a probable renewal of from one to three times. The margin required for this class of loans is also larger than for loans on feeder cattle. Since stockers are expected to be kept for growth, a loan on them is not considered as liquid as a feeder loan, but there is always a market for the stockers. Cattle-loan companies take the view that a good stocker loan to the right person is as desirable as any other. John Clay² says that a loan on stock cattle is gilt-edged when prices are advancing, but that when prices are declining nothing is poorer. It is indeed certain that although these loans are now absolutely safe, since stock can be sold at any time without a loss, a loan company must be conservative in making them. There are several cattle-loan companies that lend almost exclusively on stock cattle, and their operations over a long period of years have been entirely successful.

The third division of stocker loans is comprised of those called "summer loans." This is a special type found only in the West. Here, for example, a rancher will borrow the funds necessary to purchase a thousand head of stock cattle. He will place these on pasture during the summer and in the fall will sell the majority of them, keeping only those for which he has the necessary winter feed. These loans are considered safe, since they are for a short period of time, and since the ranches are practically all fenced.

In addition to loans on feeders and stockers, there is a third class called dairy loans, made for the purchase of dairy cows. They are long-time loans and are usually paid by monthly instalments

¹Statement made by Beverly D. Harris before the Kansas Live Stock Association, Wichita, February 9, 1916. "Cattle Paper," p. 13.

²President of the firm of John Clay & Company, Chicago.

from the proceeds of the sale of butter fat. Since they are not considered liquid and cannot be rediscounted or readily sold outside of the district in which they are made, they are very infrequently made by cattle-loan companies, and instead are usually made by local banks, which are in a better position to give them the necessary attention.

IV. THE CREDIT ANALYSIS MADE BY THE CATTLE-LOAN COMPANY

1. *Steps in the making of the loan.*—The cattle-loan company makes loans direct to the borrower and through the local bank. While many of the larger loans come direct, probably as many of the smaller ones are made with the local bank as with an intermediary. To facilitate the explanation of the steps which the cattle-loan company takes in granting a loan, it is assumed that the transaction begins with a written inquiry direct from the prospective borrower, who is unknown to the company. There are minor variations in the practices of different cattle-loan companies, but in the larger institutions, which make the major part of their loans in the range states, the process in all practical respects is the same.

After the preliminary inquiry has been made the cattle-loan company sends the prospective borrower a form for an application for a loan. This contains a brief statement as to the residence of the borrower, his general financial operations in the past and at the present, the amount of loan desired, and a detailed description of all the cattle which may be available as security for the loan. This is filled out completely, signed in the presence of a witness, and returned to the company.

If there is nothing grossly unfavorable in this application a blank financial statement is forwarded to be filled out in detail and returned. The form of the statements used by the various companies is in no two cases exactly alike.¹ These generally contain a detailed balance sheet and information concerning contingent liabilities, insurance, title to property, and references. The truth of this statement is attested before a notary public. Practically all companies require the prospective borrower to submit a financial

¹ A composite statement containing certain innovations of the writer can be found in a thesis entitled *The Cattle Loan Company*, in the University of Chicago libraries.

statement as a condition precedent to the granting of credit. There are three excellent reasons for this requirement. In the first place, all paper that is taken to a Federal Reserve bank for discount must have accompanying it a financial statement of the signer of the notes. In the second place, a statement of the borrower is necessary as a safeguard to the business. Since the loan company has loans outstanding to several times the amount of its capital and surplus, it must insist upon a substantial margin of responsibility behind the loan, otherwise a series of injudicious loans would leave the buyer of the paper "holding the bag." In the third place, there is often the same continuity of loaning in the cattle business as in commercial lines. In such cases the general financial ability of the man is very important, and a recent statement is a guide to the amount of credit to which he is entitled. As a general rule the majority of cattle raisers realize the benefit of a property statement to themselves and to the loan company and rarely object to making one of these.

The third step in the process of making a cattle loan consists in having the borrower fill out and return to the company what is known as a "brand sheet." This gives in both illustrative and descriptive form the exact holding brand on the cattle of the borrower, as well as all other brands which may be on them. One of the advantages of such a sheet consists in its accuracy. In all subsequent dealings the cattle may be identified exactly. With the aid of such a sheet the loan company determines from the county clerk in the county in which the borrower resides whether any previous loans have been made on these same cattle. The company also uses this sheet in investigating the legality of the brands given, to make sure that the brands have been registered with the county clerk, to determine that the brand given is the holding brand of the borrower, and to make sure that the legal title is clearly vested in the person seeking the loan. In the same connection the brands are investigated in the various cattle-raisers associations.

While these investigations are being made the company is investigating the general financial and moral responsibility of the man. This is true even though the cattle themselves are given as security for the loan. A factor of as great importance as integrity

and wealth is ability. It is an essential attribute of the borrower in every good loan. The most reliable sources of outside information which the loan company has in investigating the responsibility of the man are other banks. In addition, wherever it is possible the loan company investigates the general credit standing of the borrower through the various commercial agencies and through special sources.

The most reliable and capable sources are the inspectors of the cattle-loan company. These men are often stockholders in the company. In all cases they have a deep interest in the welfare of the company, and usually they are men who have been connected with all phases of cattle growing and financing. Inspectors are sent to interview a man personally before any decision is made with regard to the granting of a loan. They take note of the impression of honesty and moral responsibility the borrower gives. They note the general appearance of the place, as shown by the condition of the improvements, the fences, the soil, and the growing crops. They observe the air of thriftiness and industry, or the lack of it, that prevails about the place. They notice the general condition of the live stock on the farm and judge from it the ability of the prospective borrower as a feeder. They make sure that he has adequate facilities to care for the watering and sheltering of the added stock. They examine carefully the amount of feed which he has on hand. In general the representations made in the financial statement are verified. Finally, in all cases where it is possible the inspectors examine the cattle which the prospective borrower intends to buy with the funds to be advanced by the cattle-loan company. They note particularly their quality and condition and judge whether the price to be paid is in excess of their value. They secure the brands on these cattle and check them with the reports received from the county clerk. If the cattle are purchased in a market center instead of in the state or community where the borrower resides, then the inspection takes place there simultaneously with the purchase.

The more conservative cattle-loan companies refuse to make loans to a cattle grower who has money borrowed from other firms with other cattle of the same brand given as security. A multitude of complications may arise from these "split loans," as they are called.

In the event that the investigations of the prospective borrower made by the loan company through all the available channels, including the report of the special field man, reveal that the man is a favorable risk, consent is given to the application. The borrower may already have cattle and may wish to use the money to purchase others to augment his herd. In that case he gives a chattel mortgage on the cattle then in his possession, as well as on the ones to be purchased. If the loan company thinks that the applicant has asked for money to buy more cattle than he can handle adequately, however, it will reduce the amount of the prospective loan. It may be that the borrower has no cattle at the time and can give only the ones to be purchased as security. If he has asked for a larger loan than is warranted by the class of cattle which he offers as security, the amount again is diminished.

The interest rate which is charged, as we noted previously, varies with the class of cattle offered as security, with the conditions surrounding the loan, and with the general conditions of the money market. Since the personality of the borrower is such a large and vital force affecting the interest rate, no definite rules concerning this can be formulated. The loan company has in its concepts certain men, however, either real or imaginary, to whom they will make a loan on a certain class of cattle at a given rate, under normal conditions of the money market, with certain other conditions which they regard as ideal. Variations from these will necessitate a different rate of interest.

As soon as the amount and the rate of interest have been determined the funds necessary to the purchase of the cattle are advanced to the borrower. This may be done in a variety of ways. The Chicago Cattle Loan Company has a method that is efficient and at the same time properly safeguards the company. It advances the money by means of a "draft with a bill of sale attached." On one side of this is a draft drawn on the loan company payable to the borrower on condition that the bill of sale on the reverse side of the form is properly filled out. In this bill of sale the seller of the cattle guarantees that he has good title to them, and he surrenders this to the buyer, who is also the borrower. He further agrees that all mortgages then existing on the cattle will be

released before he can demand payment of the draft. The cattle to be sold are described in detail, and the pre-existing mortgages are listed. As a subsequent part of this same form the buyer assigns all his rights and title in the cattle to the Chicago Cattle Loan Company. The two parts are subscribed to by the signers before witnesses.

If the cattle are purchased in the market center where the loan company is located the final inspection is a simple matter and takes place simultaneously with the purchase. As is often the case, however, the cattle are purchased elsewhere by the borrower. In this event an inspector is sent to the farm of the buyer. When the cattle are delivered he inspects them to make certain that they are the same cattle that he inspected previously.

The borrower then signs either one promissory note for the entire amount of the loan, or several notes aggregating the total loan. These are also signed by a second party. In addition, a chattel mortgage on the cattle applicable to the particular state is filled out and acknowledged by the borrower as grantor and the loan company as grantee. As a general rule the contents of mortgages applying to the various states do not differ materially, but the manner of acknowledgment and filing is often different. The grantee always has absolute control over the cattle and prohibits the grantor from moving them from his premises or otherwise making any transactions affecting them without first securing its consent. Since the mortgage, to be legally effective, must conform in every respect to the requirements of the state, and since these requirements vary with the different states, it is important to ascertain carefully these essential conditions. After the mortgage is properly filled out and acknowledged it is filed with the county clerk. To safeguard itself further the company registers the mortgage, as it did the brands shown on the "brand sheet," with the cattle raisers' association of the state or district.

It is very essential that a mortgage upon the cattle be required of the borrower. In the first place, it is a proper safeguard to the final payment of the loan. Cattle are quickly movable, and the loan company is usually located at a considerable distance from the borrower. While the loan company makes a thorough investigation

and very rarely experiences difficulty with a borrower, there is always the bare possibility that a borrower will attempt to sell the cattle and abscond with the funds. Since the legal title, by virtue of the mortgage, vests in the loan company, any individual purchasing the cattle from the borrower is responsible to the lender for the proceeds. A mortgage, moreover, assures the final payment of stocker loans by giving the lender title to all the natural increase of the cattle of the borrower. In the second place, a chattel mortgage on cattle is a convenient instrument. Merchandise is usually located in the same town with the lender, and since it constitutes the stock of trade it cannot be given as security. In the case of cattle, however, intended to be kept during the life of the loan, it is no inconvenience to go through this legal safeguarding. In the third place, the mortgage provides an exact description of the security, and its registration with the county clerk and cattle raisers' association provides the machinery whereby the distant lender is able to trace the cattle if they are taken illegitimately from the premises of the borrower. Finally a mortgage is essential to effective control of the security by the cattle-loan company during the life of the loan. It gives the lender control over the feed and water of the borrower and absolute control of the cattle. If any emergency arises demanding the movement of the cattle, the loan company by virtue of the mortgage can move them immediately. Instantaneous action in this regard is often necessary to protect the company.

The cattle-loan company makes one or more inspections of the cattle between the time the loan is made and the time of its maturity. These are made usually by the same inspectors of the company that made the original investigations, the number of inspections depending almost entirely upon the borrower and the general conditions surrounding the loan. Even in the case of a new customer, if the conditions appear to be favorable, only one inspection may be necessary; while if the loan company is suspicious of the borrower and is dissatisfied with the general surroundings of the loan, several trips may be made to the farm to inspect the cattle. The district in which the borrower is located and the type of cattle loaned upon indirectly affect the number of investigations.

The essential point in all loans is for the cattle-loan company to keep sufficiently informed as to the condition of the security to know at all times that the loan is safe.

If the application for a loan comes through a local bank instead of directly to the loan company the procedure is practically the same. Although the bank has originally investigated the borrower and the conditions which surround the loan, and in addition indorses the promissory notes of the customer, in the majority of cases the loan company reinspects before it purchases the notes offered by the local bank.

2. Certain exigencies that may arise before the maturity of the loan.—There are a few possible exigencies that may arise before the loan matures. It may be that the borrower exhausts his supply of feed. In such a case, the loan company either supplies the necessary feed or markets the cattle. If it is a stocker loan and there is a shortage of grass, it may be possible to move the cattle to regions where grass is abundant. If it is a feeder loan and the cattle are in a marketable condition, it may be satisfactory to market them; if they are not, it may be better to supply the feed necessary to finish the fattening process. In any event the funds which are advanced are paid later out of the proceeds of the cattle. If a shortage of water develops, the cattle are moved to a supply when this is possible; otherwise, the only feasible plan is to rush the cattle to market.

In rare instances the loan company may become suspicious of the actions of a borrower and will market the cattle at the first favorable opportunity. It is also barely possible that a continuously falling market may indicate such disastrous results that the marketing of the cattle is the only way to prevent further losses. These examples, as we shall indicate later, are seldom encountered. There are also isolated cases where the borrowers fraudulently attempt to market the cattle given as security. This, however, is practically impossible. In the first place, the field men of the cattle-loan company are always alert for such actions. In addition there are representatives of the various cattle raisers' associations in every market in the country. Since the mortgage and the brands are registered with these associations, if cattle arrive in the market

bearing the brand which has been registered by the loan company, the representative of the cattle raisers' association notifies the company of this fact and notifies the commission firm to which they have been consigned to hold the proceeds for the cattle-loan company. If the cattle are not consigned but are sold outright, the buyer is always responsible to the loan company for the proceeds, and the borrower is liable to criminal prosecution.

There is little possibility that disease will cause any large losses in a herd. The death-rate among cattle from this cause averages from 3 to 5 per cent. The foot-and-mouth contagion causes losses of less than 3 per cent. In addition, the government pays the usual market price for animals condemned with this disease and for animals condemned with tuberculosis.

3. *Elements of strength in cattle paper.*—“As cattle sell, the loans they carry are automatically liquidated, thereby rendering such loans, in our opinion, the best investment in the world for a truly commercial bank.” Bankers and investors everywhere are beginning to realize the truth of this statement. They are beginning to see that a good cattle loan outranks even the best commercial paper, because it has many elements of security that the latter does not possess.

The most essential element of cattle paper, and probably its strongest security, is its extremely liquid quality. Cattle loans are never made for a longer time than six months. Feeder loans by their very nature liquidate themselves at the end of the period by the sale of the security. There is a continuous cash market for cattle, and market centers are located near practically every community in the United States. There is a daily cash market not only for finished beef but for every class of cattle. Thus, if the necessity arises any kind of cattle can be marketed at any time. Stocker cattle are usually not intended to be marketed until they have attained their growth, but the fact that an established cash market exists at all times makes such loans almost as liquid as feeder loans. Moreover, section 13 of the Federal Reserve Act provides that loans based upon cattle as collateral, “and having a maturity not exceeding six months,” are eligible for rediscount with the Federal Reserve banks by any member bank. This makes it

possible for a cattle-loan company to discount its paper on hand with the Federal Reserve bank if the allied bank is a member of the system. This also relieves the banker from dependence upon the markets. If for any reason he needs funds quickly he can liquidate at an instant's notice the cattle paper which he has on hand. Thus cattle paper is one of the best secondary reserves which a commercial bank can possess.

A second point of security for cattle paper is due to the fact that it is based upon a life-necessity. "Panics may come and go, prices on the stock exchange may fall with a crash, the market may be suspended and security values decline until the margins are exhausted and the principal is lost, but as long as people can obtain food they will eat, and a goodly portion of their rations will be meat, and just as the demand comes fresh every day, so there is a market every day for cattle of every description, old or young, fat or lean." The fact that the lender has legal control of the security back of the loan is an additional advantage for cattle paper. In this manner the loan company is privileged to take all of the safeguards necessary to protect the loan. Cattle paper is also strongly indorsed. In the beginning the borrower and a second party sign the promissory note. If the loan is made through a local bank, the bank places its indorsement on the note. The cattle-loan company then indorses it before it reaches the final purchaser. While the last indorsement is the only essential one from the standpoint of the final purchaser of the paper, yet the fact that all four of the indorsements are substantial and can be depended upon certainly lends prestige to the paper.

The excellent organization of the cattle industry at the present time largely removes the element of chance from cattle loans. The introduction of good business methods, winter feeding, fenced ranges, pure-bred stock, and constant supervision has transformed the business of raising cattle from a haphazard industry to one that is considered extremely safe.

There is another strong vantage-point for cattle paper in the narrow range of fluctuations in the prices of cattle over short periods of time. Some examples chosen at random clearly illustrate this point. During the first six months of 1914 there was a maximum

fluctuation in the average price of stockers and feeders of eighty cents per hundred pounds. In 1915 the average monthly prices for native steers weighing from 1,200 to 1,500 pounds fluctuated for the first six months of the year from \$7.85 to \$8.95 per hundred pounds. The range of average prices for February, March, and April, however, amounted to only five cents per hundred pounds. In 1916 the weekly average from July to December for all classes of cattle varied only \$1.30 per hundred. The extreme variations between any two weeks was fifty cents per hundred pounds, while between eleven of the twenty-seven weeks the fluctuation was not over fifteen cents. Many other similar cases could be found, but these show that large fluctuations rarely take place rapidly.

Even in years of financial panics cattle markets are little affected. The range of prices in 1907 increased in practically the same proportion over the prices of 1906 as the 1906 prices increased over those of 1905. In 1908 there was another similar advance in the range. "The packers who were purchasers of beef in the banker's panic of 1907 were embarrassed for a week or ten days only." "In the early weeks of the present war, when the securities and cotton markets were closed and the grain markets greatly hampered, all of the live-stock markets of the country were open, continuing their business on a normal basis, and at prices equal to or higher than during the months preceding." Since cattle markets and cattle prices are little affected by panics, it is logical that cattle paper itself is little affected by them. A prominent lawyer who adjusted many business failures between 1887 and 1903 says that there were smaller losses on cattle paper than on any other class of paper. J. F. Ebersole, writing on this subject, says that "holders of cattle paper have never suffered in times of financial panic from failure to pay at maturity." A representative of the firm of John Clay & Company states that in 1914, when loans based on stocks and bonds had to be continued, 96 per cent of the cattle loans of that company were paid at maturity. The fact that cattle paper has successfully weathered all of the recent financial storms is a recommendation that is hard to duplicate.

Finally there could be no more potent recommendation for the safety of cattle paper than its past infallibility in normal times. There is a large list of companies that have experienced practically no losses on loans on cattle over a long period of years. The losses of John Clay & Company, of Chicago, have been merely nominal for over ten years. The Knorpp Cattle Loan Company, of Kansas City, has not had a single loan become past due since it began business a few years ago. In three and one-half years the Portland Cattle Loan Company has lent twenty million dollars with losses of less than six hundred dollars. The St. Louis Cattle Loan Company has lost amounts aggregating only 0.00025 per cent of the total loans. Losses of the St. Joseph Cattle Loan Company covering operations of eighteen years on loans aggregating seventy million dollars have amounted to only 0.00043 per cent. This list might be continued indefinitely, but the examples of these prominent companies serve to indicate that cattle loans for the past decade and a half have been extraordinarily safe. It is only logical that paper possessed of the elements of security which we have named is rapidly becoming the most popular type of investment with banks and financiers throughout the entire country.

V. THE MARKETING OF CATTLE PAPER

Cattle loans are made in sizes varying from one or two thousand to five hundred thousand dollars. While cattle-loan companies make many small loans and indirectly finance many small borrowers by taking the surplus loans of the local banks, yet they are not primarily institutions for the small borrower, and the majority of loans in the range country will average between ten and twenty thousand dollars. There are a number of companies which make many loans of one hundred thousand dollars and more.

The cattle-loan companies keep a portion of the loans which are made. Several prominent companies always keep an amount of paper on hand at least equal to the amount of their combined capital and surplus. Apparently this plan is a safe and conservative one. It is the plan of the affiliated banks to absorb the surplus paper of the loan company at times when the smaller banks are not in the market.

The primary purpose of the cattle-loan companies is not to act as investors, however, but to serve as brokers between the investors and the cattle growers. Their methods of disposing of paper correspond in some respects to those used by mortgage-loan companies and commercial-paper houses. Unlike the commercial-paper houses the cattle-loan companies indorse the paper which they sell and take a chattel mortgage upon the security of the loan. They advance the funds to the borrower at once. The largest purchasers are probably the large eastern capitalists and eastern banks. Large commercial banks everywhere, however, are turning to cattle paper as a means of investing their surplus funds. This is especially true in the Middle West and Northwest. The large institutions, moreover, are not the only purchasers of cattle paper. In certain seasons of the year, when the farmers' capital accumulates in the banks, the small country banks invest much of their surplus in cattle paper, which they secure from cattle-loan companies. When they need their funds again the paper is probably liquidating itself by the expiration of the period of the loan. In addition to these investors cattle-loan companies sell much of their paper to the general investing public and to capitalists and financiers everywhere. In fact, any person or institution with funds that could be invested in commercial paper is a possible purchaser of cattle paper.

It is apparently the custom to sell cattle paper to investors at a rate of interest about 2 per cent less than is charged the borrower. The 2 per cent covers overhead expenses, reserve for losses, and the loan companies' profits. The large eastern banks often purchase complete loans, that is, if a loan company has notes aggregating fifty thousand dollars from a single borrower, these may all be taken by one large investor. In this case, if he so desires, a duplicate certified chattel mortgage is made out and sent along with the borrower's statement and the notes. The loans are usually, however, divided into notes of one-, five-, or ten-thousand-dollar denominations. This is to facilitate sales to small investors who do not wish to purchase amounts equal to the entire loan, and to accommodate purchasers who wish to scatter their investments among several borrowers. To eliminate the expense and labor of issuing a

duplicate certified chattel mortgage to every small purchaser of a part of a large loan, one prominent company gives the small investor what is known as a "certified trust receipt of chattel mortgage."

The purchaser of cattle paper looks to the loan company for the payment of the loan. Since the majority of companies indorse all the paper they sell, they pay the note promptly at maturity and assume themselves the responsibility of prompt payment by the borrower. There is occasionally a borrower who gets from the sale of the cattle an insufficient amount of funds to pay the entire loan. In this case he will probably pay the deficit voluntarily. In the event that he does not, the loan company must proceed legally to seize any other property which may be included in the mortgage. As a last resort, if it is necessary, the cattle-loan company may institute legal proceedings against the borrower and force the payment of the loan from his general assets. This extreme procedure, however, is rarely necessary.

Even though many investors investigate the financial and moral standing of the original borrower, they are not in a position to make a thorough analysis of the conditions surrounding the loan. Since this is the case, the purchaser of cattle paper really depends for his safety upon the stability of the company making the loan. Naturally at a time when cattle-loan companies have been multiplying rapidly, some are almost certain to be weak. Since in the event of failure an incorporated company is liable only for an amount equal to its capital, the methods of investigation, inspection, and supervision are more important than either the capital or the amount of the outstanding loans. The territory in which the major part of the company's loans are made should therefore be determined. On the basis of this knowledge it can then be decided whether adequate investigations are made, whether sufficient margins are required, whether subsequent inspections are sufficient, and whether due safeguards are taken to protect the loan. The amount of loans which an organization should have outstanding at any time depends as much upon the methods of the company as upon its capital and surplus. Some authorities claim that a conservative company using every precaution and

safeguard may lend safely from ten to twenty times the amount of its capital and surplus. Many of the best and largest companies however, feel that their loans should not greatly exceed ten times their capital and surplus. In actual practice the outstanding loans are probably never less than this amount, and in many instances reach from thirteen to fifteen times the total of the capital and surplus. There are undoubtedly some companies lending a much higher ratio than this.

The investor should also investigate the character of the institution which is allied with the loan company. An organization allied with a strong bank is certain to have a strong support in times of trouble. The integrity and ability of the men connected with the company is an even more important consideration. A company which has been operating successfully over a long period of years is always stronger than a new and untried organization.

VI. THE CORRELATION OF CATTLE-LOAN COMPANIES AND ALLIED BANKS

The national live-stock banks with affiliated cattle-loan companies have many advantages not possessed by other institutions. The loan companies themselves, moreover, are placed in a much stronger position than companies operating independently.

The chief motive prompting these banks to establish cattle-loan companies arises from their inability to make to any one person loans larger than 10 per cent of their capital and surplus. This limitation sometimes means the foregoing of very desirable business. Thus by establishing a loan company in the same building the bank equips itself with an organization that can care for those loans that are above its legal limit. Since the same men who are subscribers to the capital stock of the loan company are holders of the stock of the bank, the revenue which accrues to the loaning organization eventually finds its way into the hands of the supporters of the banking institution. It is indeed true that if the money which is used to capitalize the cattle-loan company were placed as added capital in the bank, the amount which could be lent to any one person would be raised accordingly. In the case of a bank with \$600,000 of capital and surplus and a loaning limit

of \$60,000, the addition of \$150,000 to the capital stock of the bank raises the limit only to \$75,000. If this amount is placed in a cattle-loan company, loans can be made without any limit in amount. In practice single loans of \$500,000 are sometimes made.¹ These loans are placed, moreover, at a very small cost. The officers are usually connected with the bank, and the headquarters are in the same building. There is also a very small additional office force, so that the added overhead expense comes chiefly from legal expenses, taxes, and the cost of inspection. This is only a small percentage of the profit which is made.

The second advantage is that a loan company keeps no reserves. The majority provide a certain percentage as a part of operating expenses to cover the few losses, but no reserves are required by law and none are necessary, as there are no depositors to protect. A bank, on the other hand, is required to keep an amount of readily available cash equal to from 10 to 15 per cent of the deposits of the bank. This limits the amount of loans it can make.

In the third place, the limited liability of the stockholders of a cattle-loan company may be an influence with some of the organizers. Since the majority of companies are incorporated, the stockholders of these are liable only for an amount equal to the capital stock. In a national bank, however, the stockholders are doubly liable for the amount of the capital stock. This is probably not a compelling reason for the majority of organizers, but it cannot, nevertheless, be overlooked.

Fourthly, there are certain seasons of the year in which the bank does not desire a great amount of cattle paper, because at that time there is a heavy demand for funds by the local customers. In other seasons of the year it may have a large accumulated surplus of funds to invest. It is a considerable advantage to have an affiliated cattle-loan company as a convenient source to which it can turn for cattle paper as an investment.

One of the chief benefits to a cattle-loan company allied with a strong live-stock bank is the added prestige given the company. The public always assumes that the loan company is as strong as the institution with which it is connected. This is undoubtedly

¹ In practice this does not appear to have endangered the safety of the institution.

true. There has been no crisis by which we can test the assumption, but it is certain that a failure of the allied loan company would attach a stigma to the bank as well as to the stockholders and directors. Since this would be undesirable both from a business and from a social viewpoint, the men and the institution, both usually of excellent repute, will certainly give any aid to the company which may be necessary.

In the second place, the cattle-loan company has the use of the credit machinery which has already been developed by the bank. At times when the loan company has lent what it considers a safe amount on the basis of its capital and surplus it may be able to turn many small loans to the bank and thus accommodate its customers. It has also, in the affiliated bank and especially in the bank's correspondents, a place where it can turn much of its surplus paper in dull times.

VII. THE ECONOMIC SERVICES OF CATTLE-LOAN COMPANIES

There are several economic services performed by cattle-loan companies that make them invaluable to the nation. The increased production of beef animals brought about by rendering capital available to the grower is one of the largest and most beneficial results of the operations of these companies. They began to multiply and improve at a time when production was far below the demands of consumption. This improvement made capital available to the industry at a time when the strain on the local banks was so severe that had it not been for these loan companies production must have materially decreased. On account of this service there is undoubtedly a lower price to the consumer than would otherwise have been the case.

There is a corresponding service rendered to the cattlemen. The operations of the loan companies have tended strongly to steady the price of live beef. This has been done by checking overexpansion in times of high prices and by stimulating production in times of low prices. In 1912 prices were high, and expansion to two or three times normal was imminent. The cattle-loan companies curbed this and prevented larger losses, although much was lost on the glutted market of 1913. Thus the loan companies

direct the industry to a steady expansion that can be absorbed naturally and seek to avoid periods of undue and sudden expansion, which often lead to abnormal receipts on the markets and to a heavy drop in prices to the producer.

The cattle-loan company serves both the producer of cattle and the consumer of beef by increasing the supply of available raw foodstuffs. It is impossible for any system of agriculture to succeed which does not include stock growing, for "no method of preserving soil fertility has been found that can take the place of manure." The basis of all increased production in crops must be increased fertility of the soil and improved methods of farming. Thus, since increased production of cattle means necessarily increased fertility of the soil, it directly provides larger crops of raw foodstuffs for human consumption. The increase in the yield per acre repays the farmer many times for the loss per unit of production due to the increase in supply. The increase in the available supply, on the other hand, lowers the price which the consumer must pay.

Finally the cattle-loan company renders an economic service to society by a better distribution of capital. There has been a constant tendency to concentrate capital in the industrial establishments of the nation at the expense of the producer of raw foodstuffs. This defect has been largely remedied by the activities of the cattle-loan companies. In making capital available to cattle growers the loan companies help to prevent a concentration of capital entirely in the East. Much of the money which would otherwise drift back to New York when the crop-moving season is over in the fall is turned by the loan companies into the production of finished cattle. This improvement in the distribution of capital has lowered the average rate of interest to cattlemen. The average rate charged by commission companies during the "bonanza period" of the cattle industry was 10 per cent. The strain on the local banks, moreover, was so great following this period that there was little decrease in the rates. The advent of the modern cattle-loan companies with their improved methods has had the effect of lowering the average interest rate at least 2 per cent. This saving is at least a benefit to the grower and augments his ultimate

profit. It is, in addition, a saving to the ultimate consumer, unless a monopoly somewhere intervenes to prevent the working of normal competitive forces.

VIII. THE FUTURE OF CATTLE-LOAN COMPANIES

The story of the cattle industry in the past reads like a myth to those of the present generation; the future will not fail to add its marvels. John Clay, the foremost authority on the cattle industry in America, once said: "I firmly believe that the live-stock industry is just in its infancy in this western country, and that live-stock loans will be made as long as the cattle industry exists." As long as the consumption of beef continues to be heavy and the price of beef continues to be high, there will be an increasing need for a satisfactory and mobile loan system.

The consumption of beef and beef products will probably not decrease in the immediate future. As long as the war continues, consumption is certain to be sustained at its present rate. At the close of the war the present European soldiers will again be turned into industries, but they will have to be fed, and most of the beef must be imported. This will be in addition to the call for breeding stock by the European nations.

This, however, is only a small amount in comparison to the natural demands of our own country. As long as we have wealthy people we shall have a demand for high-class beef. As long as we have industrial workers we shall have a demand for the cheaper classes of beef. While there are those who hold that a workingman can receive the proper nourishment on a diet composed entirely of vegetables, the majority of people believe that some meat is preferable in a worker's diet. The average laborer, moreover, is a firm believer in the necessity of meat as a part of his rations, and beef is his usual choice.

It seems certain that prices cannot materially decline in view of the present supply of cattle. If the number of available beef cattle increases, then the present demand may be met at a lower price. The importance of Argentine as a factor in increasing the beef supply of the United States is steadily growing less. The beef produced there, moreover, is inferior in quality and can never

take the place of corn-fed American beef. In the United States, even with the added stimulus given to the production of beef in the South, the break-up of the vast western ranges makes the increasing of the supply of beef cattle a slow process.

The requisites of a satisfactory financial institution to supply the capital essential to cattle production are most nearly found in present cattle-loan companies. It seems very clear that the Federal Farm Loan banks will not have any appreciable effect upon the cattle-loan company. The system was not intended to accommodate short-time borrowers. This act undoubtedly renders a valuable organization available to the purchaser of real estate, but it is too unwieldy and inappropriate to be of value to the cattle grower. In the first place, he may not wish a continuous loan for five years. He is often unable to give a first mortgage upon his land to secure the loan. He can usually not afford to depend upon the decisions of nine other men, nor can he afford to undergo the laborious process of investigation and appraisal which is necessary. In addition, the limit of ten thousand dollars to a single borrower places the same objection upon the Federal Farm Loan banks that the cattle-loan company was first designed to meet.

Since it has become a well-known fact to the initiated that cattle-loan companies are very profitable, it is probable that the number of these organizations will continue to increase. The natural competition between these companies will probably "weed out" those whose methods are not absolutely sound. It is probable that, although competition may drive the interest rates down, enough additional loans will be made to compensate the loss. One prominent writer says: "The four or five million dollars placed in loans yearly by the average loan company, as at present constituted, is but a fraction of the loans that may be placed by them in a few years." These companies have made notable advances in the past, and there are vast opportunities ahead.

FORREST M. LARMER

UNIVERSITY OF CHICAGO